



November 3, 2009

SUBMITTED ELECTRONICALLY

CC:PA:LPD:PR (REG-112756-09)
Room 5205
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

**Re: Proposed Amendments to Regulations Regarding Questions and Answers
Relating to Church Tax Inquiries and Examinations**

Dear Sir/Madam:

The following memorandum represents our comments and concerns regarding the proposed amendments to the Internal Revenue Service Regulations regarding church tax inquiries and examinations or IRC § 7611.

Introduction

In August 2008, the Internal Revenue Service (IRS) initiated an inquiry and subsequent tax examination of the Warroad Community Church. However, in a July 2009 letter the IRS closed the investigation citing a pending procedural issue, but reserved the right to bring a future examination to address its concerns with certain church actions.¹ The procedural issue cited by the IRS involved a district court case rejecting a petition requesting enforcement against Living Word Christian Center (LWCC).²

The IRS had received reports that LWCC had possibly engaged in prohibited political conduct, and an improper economic relationship with its pastor. As a result, the IRS issued a letter from the Director of Exempt Organizations, Examinations (DEOE) to LWCC noticing a church tax inquiry based on the DEOE's "reasonable belief" that the church's activities endangered its tax-exempt status.³ The church ultimately asserted that the inquiry had not been

¹ Letter from Sunita B. Lough, Director, Exempt Organizations Examination, Internal Revenue Service, to Warroad Community Church (Jul. 03, 2009).

² *United States v. Living Word Christian Center*, 2008 U.S. Dist. LEXIS 106639 (D. Minn. Nov. 18, 2008).

³ *Id.* at *2-3.

initiated by an appropriate IRS official.⁴ Specifically, LWCC argued that the DEOE, did not amount to an “appropriate high-level Treasury official.” The IRS then issued an administrative summons seeking several categories of information and, when LWCC failed to comply, the IRS filed an enforcement petition.⁵

In rejecting the IRS petition,⁶ the Magistrate Judge found that the DEOE was not a sufficiently “appropriate high-level Treasury official” to make the necessary reasonable belief determination to begin a church tax inquiry.⁷ According to 26 U.S.C. § 7611(h)(7), the “appropriate high-level Treasury official” is specified as either “the Secretary of the Treasury or any delegate of the Secretary whose rank is *no lower than* that of a *principal Internal Revenue officer for an internal revenue region*.”⁸ The IRS subsequently interpreted § 7611 (h)(7) to refer to the “appropriate Regional Commissioner (or higher Treasury official).”⁹

The problem arose from the restructuring of the IRS in 1998, which eliminated the former geographic regions in favor of four nationwide divisions, each covering a particular taxpayer classification. This reorganization eliminated several positions including the Regional Commissioners, whose responsibilities were purportedly delegated among other existing positions.¹⁰ The IRS, through its Internal Revenue Manual (IRM), but not through formal rule-making procedures, designated the DEOE as the “appropriate high-level Treasury official,” effectively reinterpreting § 7611(h)(7).¹¹

The court, in *Living Word Christian Center*, determined that the IRS was not entitled to the level of deference found in *Chevron U.S.A., Inc. v. Natural Resource Defense Council, Inc.*, but rather the less deferential standard of *Skidmore v. Swift & Company*.¹² Applying *Skidmore*, the court rejected the IRS’s interpretation citing the lack of formal notice and comment rule-making, which it reasoned may have allowed debate to address significant First Amendment concerns. Also, the court noted that interpreting who should be designated as a “high-level Treasury official” did not require any expertise attributable to the IRS, but was instead a question of government involvement in religious matters,¹³ a sensitive political and policy matter best handled by a senior Executive official.¹⁴

The Magistrate Judge’s opinion was later upheld by the district court. This opinion further stressed the “important constitutional interest” at risk from government “intrusion into religious affairs” and the need, evidenced by Congress’s enactment of § 7611, for a high-ranking

⁴ *Id.* at *4.

⁵ *Id.* at *4–5.

⁶ *Id.* at *43.

⁷ *Id.* at *41.

⁸ I.R.C. § 7611(h)(7) (LexisNexis 2009) (emphasis added).

⁹ *Living Word Christian Center*, 2008 U.S. Dist. LEXIS 106639, at *14–15. The definition codified in § 7611 (h)(7) was introduced with the passage of CAPA. *Id.*

¹⁰ Amendments to the Regulations Regarding Questions and Answers Relating to Church Tax Inquiries and Examinations, 74 Fed. Reg. 39,004 (Aug. 5, 2009) (to be codified at 26 C.F.R. pt. 301).

¹¹ *Id.* at 39,005.

¹² *Living Word Christian Center*, 2008 U.S. Dist. LEXIS 106639, at *15–16.

¹³ *Id.* at *29–32.

¹⁴ *Id.* at *34–35.

Treasury official sensitive to policy and political concerns to make the necessary determinations.¹⁵

In response, the IRS has requested comment on certain proposed changes to the regulations governing church tax inquiries and examinations in order to remedy ambiguities referring to positions which no longer exist after the restructuring in 1998.¹⁶ First, instead of the eliminated Regional Commissioner, the Director, Exempt Organizations (DEO) would be designated the Treasury official responsible for making the reasonable belief determination to institute a church tax inquiry and for approving the completed examiner findings on status for purposes regarding tax liability.¹⁷ In addition, the Division Counsel/Associate Chief Counsel, Tax Exempt and Government Entities would replace the Regional Counsel as the individual responsible for receiving the required notice prior to examination, filing advisory objections, approving adverse final determinations, and determining substantial compliance in certain instances.¹⁸ Finally, regarding multiple examinations, the Commissioner or Deputy Commissioner, Tax Exempt and Government Entities would replace the Assistant Commissioner (Employee Plans and Exempt Organizations) as the person responsible for giving approval for a second church inquiry or examination.¹⁹

Comments to the Proposed Amendments

The proposed changes regarding church tax inquiries and examinations raise serious concerns. Especially troubling is the proposed substitution of the Director, Exempt Organizations for the former Regional Commissioner, as the “appropriate high-level Treasury official” to make the reasonable belief determination required to begin a church tax inquiry.²⁰ This proposed substitution violates both the express language and underlying intent of the statute.

It is settled that a court must defer to a formal agency interpretation of an *ambiguous* statute, so long as that interpretation is reasonable.²¹ However, “if the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.”²² “Even for an agency able to claim all the authority possible under *Chevron*, deference to its statutory interpretation is called for only when the devices of judicial construction have been tried and found to yield no clear sense of congressional intent.”²³ Here, traditional interpretative methods do in fact yield a complete picture of congressional intent, one which the proposed rule change clearly betrays.

¹⁵ *United States v. Living Word Christian Center*, 2009 U.S. Dist. LEXIS 6902 (D. Minn. Jan. 30, 2009).

¹⁶ Amendments to the Regulations Regarding Questions and Answers Relating to Church Tax Inquiries and Examinations, 74 Fed. Reg. at 39,003.

¹⁷ *Id.* at 39,005–6.

¹⁸ *Id.* at 39,005.

¹⁹ *Id.* at 39,006.

²⁰ *Id.* at 39,005.

²¹ See *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 476 U.S. 837 (1984).

²² *Id.* at 843.

²³ *Gen. Dynamics Land Sys. v. Cline*, 540 U.S. 581, 600 (2004).

1. Allowing the Director, Exempt Organizations to Make the Necessary Reasonable Belief Determination Violates the Clear Statutory Language.

First, under the Plain Meaning Rule, “[i]t is elementary that the meaning of a statute must, in the first instance, be sought in the language in which the act is framed, and if that is plain, . . . the sole function of the courts is to enforce it according to its terms.”²⁴ In this instance, 26 U.S.C. § 7611 provides that, before a church tax inquiry may begin, “an appropriate high-level Treasury official [must] reasonably believe[] . . . that the church may not be exempt, by reason of its status as a church . . . or may be carrying on an unrelated trade or business . . . or otherwise engaged in activities subject to taxation.”²⁵ Additionally, 26 U.S.C. § 7611 (h)(7) further defines “an appropriate high-level Treasury official” as “the Secretary of the Treasury or any delegate of the Secretary whose *rank is no lower* than that of a principal Internal Revenue officer for an internal revenue region,”²⁶ which the IRS later interpreted to refer to the now defunct Regional Commissioner position.²⁷ Based upon the statute’s language, the elimination of the Regional Commissioner does not itself render the statute ambiguous.

As previously discussed, the statute charges that the principal officer of a region is the *lowest* ranking, not the only, Treasury official entitled to make the required determination.²⁸ Congress actually directed the IRS to place the determination power in the Treasury chain-of-command between the Treasury Secretary and “a principal Internal Revenue officer for an internal revenue region.”²⁹ Again, it was the IRS which chose the latter and subsequently designated the principal officer to be the Regional Commissioner. The IRS could have instead chosen to place determinative authority in another individual allowed under the statute. The mere elimination of one choice which the statute provides for does not render the entire range of choices or the statute itself necessarily ambiguous.

By simply referring back to the statute and following its direction, the IRS could easily avoid any potential conflict. Obviously, offices exist which possess higher level authority than a Regional Commissioner and the statute is clear that vesting determinative authority in these offices would be sufficient to provide the necessary constitutional safeguards. The most obvious way to give effect to the statute is to vest the determinative authority in the Treasury Secretary, the specific official to which it refers.³⁰ In the alternative, the Commissioner of the IRS would also be a permissible choice. As the most senior officer at the IRS, the Commissioner was obviously within the contemplation of Congress during the drafting of the statute. Therefore, to follow the clear direction of the statute, the IRS should designate one of these individuals to make the required determination.

²⁴ *Caminetti v. United States*, 242 U.S. 470, 485 (U.S. 1917).

²⁵ I.R.C. § 7611(a) (LexisNexis 2009).

²⁶ *Id.* § (h)(7) (emphasis added).

²⁷ Amendments to the Regulations Regarding Questions and Answers Relating to Church Tax Inquiries and Examinations, 74 Fed. Reg. at 39,004. This position was also suggested by the legislative history. *Id.*

²⁸ See I.R.C. § 7611(h)(7) (LexisNexis 2009).

²⁹ *Id.*

³⁰ See I.R.C. § 7611(a) (LexisNexis 2009).

2. Allowing the Director, Exempt Organizations to Make the Necessary Determination Violates the Clear Intent of Congress.

Even if a purely textual examination of the statute did not resolve all supposed ambiguity, Congress's clear intent most certainly does. In 1985, the IRS published an article explaining the changes to church audit procedures. The article's introduction outlines the specific congressional concerns which led to a revision of church audit procedures. Chief among them was the desire "to protect churches from undue interference by the IRS" and maintaining the delicate constitutional balance while resolving problems involving church and state separation.³¹ While certain protections already existed, these were too obscure and reliant upon IRS internal policy to sufficiently "protect the rights of a church in the examination process."³²

Consequently, Congress sought to address its concerns by ensuring that the IRS official tasked with making the necessary determination to conduct a church inquiry or examination possessed a particularly "heightened political and policy sensitivity" which would allow proper balancing of First Amendment protections with the need for law enforcement.³³ To this end, Congress provided a choice of individuals with broad management authority, who were high-level politically savvy officials.³⁴ While the IRS's delegation of responsibility to the Regional Commissioners met this standard, a downward delegation to the more narrowly-tailored position of Director, Exempt Organizations does not. Regional Commissioners supervised implementation of a wide range of IRS policies over large geographic areas and were responsible to the Commissioner of the IRS.³⁵ By contrast, the Director, Exempt Organizations (DEO) does not possess such broad authority and does not significantly differ from the Director, Exempt Organizations, Examinations (DEOE), a position previously rejected by the district court.³⁶ While the office is part of a national division, the authority of the DEO, and the division itself, is much more limited in scope than a Regional Commissioner's, since the DEO's authority exclusively involves only tax exempt organizations. This compartmentalized exposure does not provide the same necessary background or broad appreciation for balancing various delicate issues, especially important constitutional ones. To select an individual subject to so many levels of management supervision and possessing such a limited scope of influence and authority clearly violates Congress's intent in passing the statute. On the other hand, appointing an individual such as the Treasury Secretary or the Commissioner of the IRS obviously fulfills congressional intent, and represents the heightened level of approval needed "to protect churches from undue interference by the IRS" and to maintain the delicate constitutional balance involving church and state separation.³⁷

Another possibility for fulfilling legislative intent might seem to lie in discerning the current equivalent of the former Regional Commissioner and assigning the disputed responsibility accordingly. However, such a determination may prove difficult or unworkable.

³¹ Internal Revenue Service Exempt Organizations, Deficit Reduction Act of 1984: Church Audit Procedures (1985), available at <http://www.irs.gov/pub/irs-tege/eotopicp85.pdf>.

³² *Id.*

³³ *Living Word Christian Center*, 2008 U.S. Dist. LEXIS 106639 at *34-35.

³⁴ *Id.* at *38-39.

³⁵ *Id.*

³⁶ *See Id.*

³⁷ *See*, note 31, *supra*.

Under the present IRS structure, Divisional Commissioners, which head each of the four major IRS divisions, would seem to be the hierarchical equivalent of Regional Commissioners, a fact evidenced by the district court.³⁸ While delegation to this position might seem logical, it is, in reality, somewhat problematic. First, as previously stated, the statute clearly provides a range of individuals Congress believed were sufficiently qualified to make the necessary determinations, a range which expressly does not include the newly established Divisional Commissioner. Also, since the divisional structure did not exist when the statute was passed, Congress was not able to pass judgment or approve the qualifications of the Divisional Commissioner to make necessary church inquiry or audit determination. Furthermore, the Divisional Commissioner position suffers from largely the same compartmentalized limitation which befalls the DEO. Although, the Divisional Commissioner's realm of authority is relatively larger than that of the DEO's—including employee plans and government entities in addition to exempt organizations³⁹—it is still far more limited than the former Regional Commissioner, and as likely does not possess the necessary policy and political sensitivity. Under the current structure, there seems to be no equivalent, at least with regard to political and policy sensitivity, to the Regional Commissioner, which directs the agency back to the previously discussed solution of the Treasury Secretary or Commissioner of the IRS.

Lastly, selecting the Divisional Commissioner could prove only a temporary solution. Throughout its existence, the IRS has often been structurally reorganized.⁴⁰ As previously discussed, it was the elimination of certain positions through such a reorganization which served as the catalyst for the proposed revisions. Given this history, it is likely that the agency could be reorganized again or, at least, certain positions may be eliminated, which could include Divisional Commissioners. This problem is easily remedied by delegating the determination, as previously explained, to either the Treasury Secretary or the IRS Commissioner. Unlike the Divisional Commissioners, these offices were statutorily created and thus are not subject to elimination through an internal reorganization.⁴¹

Conclusion

Allowing the Director, Exempt Organizations, to make the necessary reasonable belief determination to initiate a church tax inquiry or audit is in stark contrast to both the language of the statute and legislative intent. The statute clearly provided that the IRS could have chosen between several individuals from which the agency selected the Regional Commissioner. Despite the elimination of that position, the statute leaves the IRS with clearly directed alternatives from which to select a qualified replacement to perform the required determination. Therefore, the mere elimination of Regional Commissioners does not cause an ambiguity requiring deference to the agency's choice of an unprovided alternative. Indeed, the IRS should be required to choose, as the statute provides, only those offices specified as possessing the necessary policy and

³⁸ *Living Word Christian Center*, 2008 U.S. Dist. LEXIS 106639 at *37.

³⁹ <http://www.irs.gov/irs/article/0,,id=100971,00.html>

⁴⁰ Letter from Sen. Max Baucus and Sen. Charles Grassley, United States Senate Committee on Finance, to Mark Everson, Commissioner Internal Revenue Service (June 23, 2003), *available at* <http://finance.senate.gov/press/Bpress/2003press/prb071003.pdf>.

⁴¹ I.R.C. § 7803 (LexisNexis 2009); 31 U.S.C.S. § 301 (LexisNexis 2009).

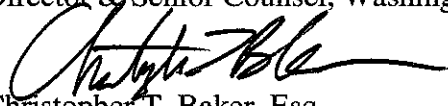
political understanding needed to protect and properly balance the sensitive church/state constitutional and statutory issues.

Moreover, based on the statutory language and Congress's clear intent, the most direct way for the IRS to ensure its compliance is to appoint a senior Treasury officer with statutory-based authority, such as the Treasury Secretary or the Commissioner of the IRS. The downward delegation to a position with less authority or political sensitivity will place in danger the very constitutional considerations Congress sought to protect. Accordingly, the proposed rule changes should be rejected in favor of those positions specified by statute.

Sincerely,



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